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RUEHBJ/AMEMBASSY BEIJING 2736  
RUEHRL/AMEMBASSY BERLIN 1374  
RUEHLO/AMEMBASSY LONDON 2012  
RUEHFR/AMEMBASSY PARIS 6046  
RUEHFT/AMCONSUL FRANKFURT 0475  
RUEHFK/AMCONSUL FUKUOKA 7188  
RUEHOK/AMCONSUL OSAKA KOBE 0857  
RUEHKSO/AMCONSUL SAPPORO 7782  
RUEHGH/AMCONSUL SHANGHAI 0384  
RUEHBS/USEU BRUSSELS  
RUEHGV/USMISSION GENEVA 3287

C O N F I D E N T I A L SECTION 01 OF 02 TOKYO 000977

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TREASURY FOR DOHNER, POGGI; STATE FOR EEB/OMA AND EAP/J;  
NSC FOR TONG;

E.O. 12958: DECL: 04/19/2018

TAGS: [EFIN](#) [ECON](#) [PGOV](#) [JA](#)

SUBJECT: BANK OF JAPAN: SHIRAKAWA AT LAST

REF: A. TOKYO 801

[1](#)B. TOKYO 761

Classified By: CDA M. Meserve for reasons 1.4 b/d

#### Summary

[1](#)1. (C) Japan's ruling coalition and leading opposition party finally agreed on a candidate to fill the post of central bank chief April 9, endorsing Deputy Governor Masaaki Shirakawa. Shirakawa was named one of the two deputy governors March 19, and served as Acting Governor during the three week governorship vacuum period, as the previous governor's term ended without a replacement, due to political fighting in the Diet. Monetary policy should remain consistent with the approach taken under former Governor Fukui. The impasse over the Bank of Japan appointments has placed serious stresses on the Fukuda administration and on the two major political parties. It also showcased Japan's current Diet dynamics in a most unflattering light for the international community. End Summary.

#### Shirakawa In, Watanabe and Any Other MOF Figures Out

[1](#)2. (U) Having endorsed Shirakawa as Deputy Governor in March, the main opposition Democratic Party of Japan (DPJ) went along April 9 with his nomination to the top job. However, the ruling coalition's attempt to place former MOF Vice Minister Hiroshi Watanabe into Shirakawa's vacant Deputy Governor slot was blocked by the DPJ. Recently, DPJ President Ozawa publicly announced he was fundamentally opposed to former MOF bureaucrats assuming positions at the BOJ. However, Prime Minister Yasuo Fukuda evidently wished to continue the tradition of including top figures in the bank with links to MOF, academia, and the private sector. Given the DPJ's control of the Upper House, Watanabe's opportunity to take Shirakawa's vacated position fell short; the Deputy Governor slot will remain vacant for the time being.

Fukuda, Ozawa Both Damaged, but DPJ Holds Firm

¶3. (C) The April 9 plenary votes went largely along party lines, with only a few DPJ defections, belying major disagreements within the DPJ over Watanabe's nomination. Earlier that morning, most major dailies had described the main opposition party as in "serious disarray" over the issue, noting that party leaders were resorting to heavy-handed tactics to enforce party discipline. A few reports suggested Ozawa was losing his grip on the party, and labeled the Watanabe votes a referendum on his leadership. Shortly after the votes, the media proclaimed Ozawa firmly in control. Some reports suggested DPJ leaders feared a reprise of Ozawa's November 2007 resignation over a proposed "grand coalition" with Fukuda's ruling Liberal Democratic Party (LDP). An Embassy media contact said that while a majority of DPJ members may have supported Watanabe's nomination, they decided in the end to put the priority on party unity, recognizing that there is no suitable alternative to Ozawa at this time. Prime Minister Fukuda, for his part, has drawn sharp and repeated criticism, including from some in his own party, for insisting on successive nominees with MOF backgrounds. His support in public opinion polls has dropped sharply over the past several weeks.

#### Policy Normalization, If Normal Holds

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¶4. (U) Although Shirakawa evinced a preference for policy normalization in a September 3, 2007 interview with the Nikkei, in which he stated, "(I)f the view spreads that the call rate will remain indefinitely low in contrast to the economic realities...I would not rule out the possibility of too much fluctuation in the economy and prices," during his April 8 Diet confirmation hearing, he asserted, "(The

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important thing is) not to hold prejudgments but to carefully examine the probability of forecasts and the risk factors on both the upside and downside, resulting in flexible implementation of policy as needed and as appropriate," suggesting that he is not ruling out future rate cuts, depending on conditions. Market analysts reading these tea leaves suggest that he has taken a less hawkish stance in view of recent market developments.

#### Market Response

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¶5. (U) In his first Policy Board meeting as Governor, Shirakawa left the key overnight rate at 0.5 percent, as the BOJ cautioned, "Japan's economic growth is slowing, mainly due to the effects of high energy and materials prices." The Nikkei average closed down 1.1 percent, and Japanese government five, 10, 20, and 30 year bond yields all closed up slightly on reduced expectations of a BOJ rate cut.  
SCHIEFFER